FAB ESG WEEKLY UPDATE

31 March 2023 – 57th edition

This week, we identified the following events of significance within sustainability and their respective business implications.

For previous editions please refer to our website repository.

REGULATORY:

1. The **European Central Bank (ECB)** published its first climate-related financial disclosures. The disclosure of portfolios on road to Paris-alignment provides information on the carbon footprint of ECB's portfolios and their exposure to climate risks, climate-related governance, strategy, and risk management. It also shows that the ECB has more than halved emissions from corporate and equity investments in its staff pension fund since 2019. For its own funds' portfolio, the ECB has gradually increased the share of green bonds, up from 1% in 2019 to 13% in 2022.

- The disclosures illustrate that the corporate bonds held under the corporate sector purchase programme (CSPP) and the pandemic emergency purchase programme (PEPP) are on a decarbonisation path. Although the portfolios' absolute greenhouse gas emissions have increased in recent years because the Eurosystem has purchased more securities for monetary policy purposes, issuers' carbon intensity has gradually declined. This is partly due to the fact that the companies in ECB's portfolio have lowered their emissions for every million euro of revenue they earn, reflecting their efforts to significantly reduce emissions and boost carbon efficiency.
- From now on, the ECB will disclose climate-related information on these portfolios every year, while continuously improving the disclosures as the quality and availability of data progress. Over time, the regulator will expand the scope of the disclosures to cover other monetary policy portfolios, such as those under the public sector purchase programme (PSPP), the third covered bond purchase programme (CBPP3) and other assets under the PEPP. The ECB also aims to set interim decarbonisation targets for its own funds' portfolio and staff pension fund to stay on track with Paris Agreement goals.

2. The **U.K. Financial Conduct Authority (FCA)** communicated a push back on the introduction of anti-greenwashing sustainability disclosures and labeling rules for investors. The British regulator updated the timing of its sustainability disclosure requirements (SDR) and investment labels consultation. In order to take account of the significant response received to its consultation of the new rules, the FCA intends to publish the policy statement in Q3 2023, instead of the first half of the year.

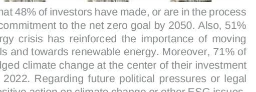
- The FCA confirmed that its upcoming policy would not require independent verification of product categorization to qualify for a label. Additionally, the regulator indicated that the rules would allow for measures to accommodate products that may not qualify for a label, but nevertheless have some sustainability-related characteristics.
- The regulator sought international coherence with other regimes and will continue to consider how to further support compatibility, while emphasizing that robust standards are needed for the U.K. to remain at the global forefront of sustainable investment. A strengthened regulatory framework for these products will increase opportunities and competition in the market, while helping foster growth, the demand and supply of products that better suit consumers' needs and preferences.

3. The **European Union (EU)** announced 100% carbon dioxide emission reductions for both new cars and vans from 2035. The EU also established a goal of 55% carbon dioxide emission reductions for new cars and 50% for new vans from 2030 to 2034, compared to 2021 levels. The new rules aim to reduce emissions from road transport that has the highest share of emissions from transportation and provide the right push for the automotive industry to shift towards zero-emission mobility, while ensuring continued innovation in the industry.

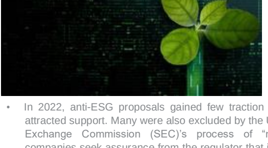
- The regulation contains a reference to e-fuels. After a consultation with stakeholders, the European Commission will make a proposal for registering vehicles running exclusively on emission-neutral fuels, after 2035, in conformity with EU law, outside the scope of the fleet standards, and in conformity with the EU's climate neutrality objective. The regulation includes a review clause that foresees that in 2026, the Commission will thoroughly assess the progress made towards achieving the 100% emission reduction targets by 2035 and the possible need to review them.
- A regulatory incentive mechanism for zero and low-emission vehicles (ZLEV) will be in place from 2025, until the end of 2029. As part of this mechanism, if a manufacturer meets certain benchmarks for the sales of zero and low-emission vehicles, it can be rewarded with less strict emission targets. The benchmark is set at 25% for cars and 17% for vans.

RESEARCH

1. Robeco published a report stating that **investors continue climate change efforts despite headwinds**. According to the results of Robeco's 2023 climate survey of 300 investors, climate change is a significant part of their investment policy and has remained stable at above 7 in 10. The desire to protect biodiversity is becoming mainstream among 47% of the surveyed investors, and enthusiasm for investing in renewables is growing, as the survey revealed a clear shift in the focus moving from aspiration to implementation. Green bonds, for example, are seen as ideal for the integration of biodiversity issues into portfolios over the next 1 to 2 years.



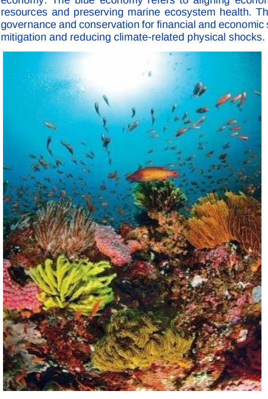
- The survey showed that 48% of investors have made, or are in the process of making, a public commitment to the net zero goal by 2050. Also, 51% stated that the energy crisis has reinforced the importance of moving away from fossil fuels and towards renewable energy. Moreover, 71% of investors acknowledged climate change at the center of their investment policy, from 75% in 2022. Regarding future political pressures or legal actions for lack of positive action on climate change or other ESG issues, concerns were felt by 63% of European investors, 57% of Asia-pacific investors and 47% of North American investors. The Paris Agreement target seems achievable for 38% of the surveyed investors.
- Sentiment was hurt by a number of headwinds, led by greater geopolitical uncertainty following Russia's invasion of Ukraine. This added to inflationary pressures and triggered an energy price spike, particularly in Europe, leading some investors to pause or revise plans to move away from fossil fuels in the short term. Investors are encountering political pressure through an anti-ESG movement that has become more vocal against the use of ESG factors in investment decisions. A significant divergence has emerged between the U.S., where anti-ESG protagonists argue that it cuts into returns, and with Europe and Asia-Pacific, where investors conversely fear the consequences of not using sustainability factors.



2. As You Sow issued a report highlighting that **anti-ESG proposals are up 60% this year, despite low support in 2022**. At least 43 anti-ESG proposals have been put to companies so far in this proxy season, from 27 anti-ESG proposals filed last year. The majority of proposals against ESG issues questioned the wisdom of racial and ethnic board diversity, while suggesting that diversity, equity, and inclusion (DE&I) programmes and anti-racism initiatives discriminate against conservative white people.

- In 2022, anti-ESG proposals gained few traction and less than 4% attracted support. Many were also excluded by the U.S. Securities and Exchange Commission (SEC)'s process of "no action" where companies seek assurance from the regulator that it will not act if they do not allow shareholders to vote on it at their next annual meeting. As an example, 6 anti-ESG proposals submitted by the conservative think-thank the National Centre for Public Policy Research (NCPPR) were excluded in 2022.
- Investors have filed 542 shareholder proposals so far for the 2023 proxy season, about even with last year at this point in 2022, when by year's end a total of 617 had been filed. Additional proposals for spring votes will show up as the season progresses and more will be filed for meetings that occur after June. Thirty proposals are included in the aggregate totals but not described in detail since they have yet to be made public by the proponents.

3. Marine Policy authored an article analysing how **blue financing can sustain ocean conservation and development**. The study presents a benchmark of the blue finance mechanism that can be used to create stable channels of finance and active investment markets in marine conservation to close the financing gap in the blue economy. The blue economy refers to aligning economic growth and stability with the sustainable use of ocean resources and preserving marine ecosystem health. The article outlines the vital importance of sustainable ocean governance and conservation for financial and economic stability, due to the central role oceans play in climate change mitigation and reducing climate-related physical shocks.



- The article recommends a legal framework incorporating blue economy principles and providing multi-stakeholder regulatory incentives for financing sustainable ocean governance. This includes national and international regulation designed to facilitate relationships between investment and marine conservation by requiring profitable ocean industry projects to purchase blue bonds, with returns guaranteed by development banks and global funds. It also recommends that blue finance mechanisms are structured to encourage partnerships between private investors, governments, global funds, and banks.
- Around 82% of global carbon deposits are stored in the ocean, highlighting the urgent need to mobilize finance to address deteriorating ocean health. Linking sustainability outcomes to profitable ocean activities such as offshore wind can create bankable opportunities that stimulate economic development and allow ocean-related developers to double their profits on returns from a blue bond. In the future, key factors that must be expanded by regulators, researchers, and policymakers, including the design of financing structures, research and development, data availability and quality, sustainable investment principles, and impact monitoring assessments.

COMPANIES

1. The **International Accounting Standards Board (IASB)** initiated a project to consider climate-related risks in financial statements. The established work plan aims to explore whether and how companies can provide better information about climate-related risks in their financial statements. The initiation of the project responds to feedback received from the IASB's recent consultation to enhance the reporting of climate-related risks in the financial statements.

- In undertaking the project, the IASB will consider the work of the International Sustainability Standards Board (ISSB) to ensure any proposals work well with IFRS sustainability disclosure standards and that any information required by the two boards would be complementary. The first two IFRS sustainability disclosure standards are due to be issued by the end of Q2 2023.
- The project was discussed at the IASB meeting for the first time. It will research to what extent the educational material published in 2020 is helping companies reflect the effects of climate related risks in the financial statements, and what actions, if any, the IASB could take to further improve information about these matters.

2. Race to Zero launched a new tool to enhance transparency of net zero commitments. Among several findings backed by the new tool, Race to Zero concluded that nearly two thirds of 500 companies have published a plan to get to net zero emissions by 2050. Also, around 90% of companies have set a specific date for their net zero target, over 70% have an absolute interim target by 2030 and around three quarters of the companies are disclosing through CDP.

- The new tool also highlighted that 393 companies published historical emissions data. Their emissions are falling at a mean rate of -6.45% per year over the 2019-2021 period, based on the companies' direct (scope 1) and indirect (scope 2) emissions. What the tool reveals are significant differences in the quantity and quality of data published by the 500 companies. Most striking is the lack of consistency of reporting for scope 3 emissions, which looks at the full value chain of a company. Out of a total of 15 scope 3 categories, about 30% of companies are reporting 3 categories or fewer, thereby not reporting on the full impact of their companies' activities.
- Data explorer is a tool showcasing climate data from the largest 500 companies in the campaign. The data explorer is a critical first step in enhancing the transparency of net zero commitments. It was developed by Climate Arc and is powered by data from the world's largest environmental disclosure system, CDP. The tool tracks the progress of companies in meeting the Race to Zero criteria, including the pace of emissions reductions. The Race to Zero data explorer is a contribution to the Global Stocktake process this year, which aims to assess the world's collective progress towards achieving the long-term goals of the Paris Agreement.

3. The **European Financial Reporting Advisory Group (EFRAG)** announced a **delay of the sector-specific European sustainability reporting standards (ESRS)**. European Union (EU) Commissioner Mairead McGuinness publicly called on EFRAG to prioritize its efforts on capacity building for the implementation of the first set of ESRS over the preparatory work for the draft sector-specific standards. The move aims to avoid overlapping consultations and eases the burden on all stakeholders wanting to contribute to the sustainability agenda. EFRAG is adjusting its workplan to this new priority, whilst carrying on under a modified timetable work on sector-specific standards and standards for SMEs.

- EFRAG delivered the first set of draft ESRS to the European Commission covering the sector-agnostic standards in November 2022. Following Commissioner McGuinness' call, EFRAG fully recognized the need to translate a legal and regulatory framework into a real operational success and does not underestimate the significant potential challenges that are faced by all stakeholders. As a consequence, EFRAG is discussing how to put in place, with a high priority, an ESRS implementation support function.
- This could be organized under three pillars: the swift and timely provision of much-needed guidance; the creation of a user-friendly and comprehensive documentation hub; and the facilitation of educational initiatives. EFRAG is actively working on the digitalization of the first set of ESRS. The following sets of the ESRS draft, dedicated to SMEs and sector-specific standards, remain on EFRAG's agenda as a key task.